Production Revenue Administration

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Priority Mail
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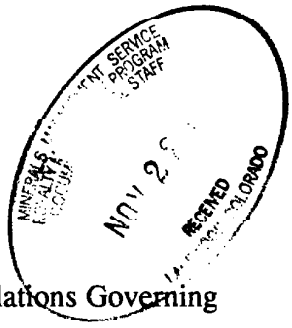

Dear Mr. Guzy:

RE: Comments on Proposed Rulemaking - Amendments to Regulations Governing Valuation of Natural Gas Produced from Indian Leases

Marathon appreciates the opportunity to comment on the MMS' Notice of Proposed Rulemaking (NOPR) governing valuation of gas produced from Indian leases. This NOPR was published in the September 23, 1996 Federal Register (Volume 61, Number 185).

Marathon would like you to consider the following comments regarding the NOPR:

General Comment

The use of independent published index prices and the alternative "percentage bump" method of valuation would provide a benefit to the MMS and industry by adding certainty to their auditing and administrative role for the Indian lessor; however, the implementation of a safety net eradicates any potential improvements.

Specific Comment

Section 202.550 (a), MMS requests comments on whether the department should provide approval for allotted leases when a lessee, who demonstrates economic hardship, may request a royalty rate reduction on an allotted lease. Marathon believes the MMS should continue to provide the necessary decision and approval process in the interest of an allottee lessor.

Section 202.550 (b), how to pay royalties on takes vs. entitled share not in an Approved Federal Agreement (AFA). The takes basis would appear to only be approved by the MMS when all working interest owners have the same Indian royalty burden, thereby ensuring the Indians receive their entitled share in a timely manner. Marathon agrees that royalties can be paid on a takes basis in an AFA once the approval process is in place, however, prior to that time, Marathon continues to assert that royalties should be paid on an entitlements basis as mandated by the existing March 1, 1988 regulations.

Section 206.170 (c), royalty valuation provisions. Marathon agrees that a lessee and tribal lessor can effectively negotiate valuation methods between themselves; however, the MMS would need to negotiate on behalf of the allottee Indian lessors.

Section 206.172, how to determine value in an index zone. This section provides for two safeguards ensuring the index value represents market value. Marathon believes the index-based formula would satisfy both the gross proceeds and major portion provisions in most Indian leases. The MMS' inclusion of an unnecessary additional calculation would further administratively burden industry by the requirement to track gas sales beyond the first index pricing point. The MMS is requiring industry to break the confidentiality clause contained in many gas contracts between buyer and seller by requiring a payor to calculate a weighted average price on gas sales from Indian, Federal, State and fee properties.

The "safety net" provision in the rule negates any certainty and simplicity for industry or MMS. Marathon objects to tracing gas and believes that this provision of the rule will be impossible to satisfy with any certainty and will inevitably lead to the current cycle of endless audit disputes and litigation with regard to gas valuation on Indian leases.

The index-based formula will yield a value that is far in excess of market value. This formula price should satisfy the gross proceeds and major portion clauses of an Indian lease without any need for a "safety net" provision on non-dedicated sales. The "safety net" provision, to tie value to markets downstream of an index point, implies a duty to market even further from the field or area and is highly objectionable. A lessee's duty to market gas, contained in the standard Indian lease, ends at or near the lease, not some point downstream of the lease.

Section 206.174, requires a "minimum value" for gas plant products when a lessee chooses to perform an actual dual accounting calculation. A minimum value method for gas plant products is not required or suggested by the lease terms. The formula pricing satisfies the major portion requirements for the entire gas stream and not just the methane portion.

Section 206.178, the elimination of Form MMS-4295 and support information for transportation allowances. Marathon agrees with the elimination of the filing for pre-approval to deduct arm's-length transportation allowances. This form does not establish validity of the transportation allowance. Furthermore, Marathon contends that transportation contracts, invoices, or non-arm's length transportation cost documentation should be made available only upon audit and review.

MMS requests comments on several specific questions related to this proposal. Comments are as follows:

Is a Minimum value needed when a lessee chooses the actual dual accounting methodology?

- Marathon believes such a provision is neither required by the lease terms nor a desirable part of this rule.

Are Conway and Mt. Belvieu the proper locations to look for prices for gas plant products?

- The proper location for gas plant product values is the point at which the products are sold.

Are the $.07 and $.08 per gallon the right deductions for transportation and fractionation?

- The major portion calculation for liquids within the actual dual accounting calculation is neither desirable nor necessary, therefore rendering the issue of deductions for transportation and fractionation as irrelevant.

Would a percentage of the price or actual rates paid be a better deduction?

- As referenced above, we consider these issues irrelevant when used in the above context.

The Paperwork Reduction Act

- MMS requests comment on two new forms, MMS-4410 and MMS-4411.

- Marathon believes Form MMS-4410 is not necessary. In addition, the certification portion and record keeping will be administratively burdensome.

- Marathon believes Form MMS-4411 is not necessary, because the entire "safety net" concept is not acceptable.

- The preamble to the rule states "only a minimal record keeping burden would be imposed annually by this collection of information" is inaccurate. The compliance requirements to this rule will force companies to institute entire new accounting procedures and systems and create additional record collection and storage for purposes of audit.

Once again, Marathon thanks you for the opportunity to provide comments to this proposed rule. If you have questions regarding our comments, please contact Linda Brown at 419-421-2457.

Very truly,

Dow L Campbell

Dow L. Campbell
Attorney

DLC/LGB/srh
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